

MOTION DUE
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No. 85-599

In the Supreme Court
OF THE
United States

OCTOBER TERM, 1985

UNITED STATES OF AMERICA,
Petitioner,

vs.

AMERICAN BAR ENDOWMENT, et al.,
Respondents.

On Writ of Certiorari to the
United States Court of Appeals for the Federal Circuit

MOTION OF
CALIFORNIA FARM BUREAU FEDERATION
FOR LEAVE TO FILE BRIEF AMICUS CURIAE,
AND BRIEF AMICUS CURIAE
IN SUPPORT OF RESPONDENTS

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CALIFORNIA FARM BUREAU FEDERATION
FOR LEAVE TO FILE BRIEF AMICUS CURIAE
IN SUPPORT OF RESPONDENTS

California Farm Bureau Federation respectfully moves the Court for leave to file the accompanying brief *amicus curiae* in support of Respondents' position in this case.

INTEREST OF
CALIFORNIA FARM BUREAU FEDERATION

California Farm Bureau Federation is a voluntary, non-governmental, nonprofit California corporation. Its primary purpose is to protect and foster agricultural interests throughout the State of California. Its members consist of 53 county Farm Bureaus with a combined membership at the close of its 1985 membership year

of over 98,000 families. Over 85% of all commercial farmers in the State of California are members of county Farm Bureaus.

At all times since August 29, 1930, California Farm Bureau Federation has been exempt from taxation under I.R.C. § 501(c)(5) and its predecessors as an agricultural organization. As such, California Farm Bureau Federation seeks the Court's permission to express its view in this case because the Court's disposition of a central question herein could have a significant impact on the operation of two important group insurance programs which it offers to members of its member county Farm Bureaus; those programs involve workers' compensation insurance and health insurance. That central question, of course, is whether proceeds realized by a tax-exempt organization from its group insurance activities constitute unrelated business income subject to taxation under I.R.C. §§ 511 through 513.

SUMMARY OF THE BRIEF AMICUS CURIAE

The accompanying brief *amicus curiae* summarizes the manner in which the workers' compensation and health insurance programs of California Farm Bureau Federation are operated and discusses the importance of these programs to it, its member county Farm Bureaus and their member families.

The brief *amicus curiae* also discusses a key difference between respondent American Bar Endowment's group life insurance program and the workers' compensation insurance program of California Farm Bureau Federation. That difference pertains to the relation of each organization's group insurance activities to their respective tax-exempt purposes. The American Bar Endowment evidently has conceded that its group insurance activities are not substantially related to its tax-exempt purposes, whereas the group workers' compensation insurance activities of California Farm Bureau Federation are an integral part of its *raison d'être*. The brief *amicus curiae* thus urges that the Court not address this peripheral issue in the case at bar.

Respondent refused its consent to the filing of the accompanying brief *amicus curiae*.

REASONS FOR GRANTING THIS MOTION

California Farm Bureau Federation is only one of perhaps thousands of nonprofit organizations which engage in group insurance activities for the benefit of their members. Its own group insurance activities are probably typical of those of many other nonprofit organizations.

California Farm Bureau Federation believes that the Court should be apprised of the nature, operations and importance of its group insurance programs, so that the Court may understand the impact which its decision in the case at bar might have on these programs, as well as on the countless similar programs operated by other nonprofit organizations throughout the country.

Moreover, California Farm Bureau Federation points out for the Court that at least some group insurance programs sponsored by nonprofit organizations, including its own, are substantially related to the tax-exempt purposes of those organizations. California Farm Bureau Federation believes that the Court should conclude that it should not address this peripheral issue in the instant case, but should defer it for adjudication, if necessary, upon a fully developed record and briefing by an organization to which it is of the greatest importance.

WHEREFORE, California Farm Bureau Federation respectfully moves the Court for leave to file the accompanying brief *amicus curiae*.

Respectfully submitted,

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**BRIEF AMICUS CURIAE
OF CALIFORNIA FARM BUREAU FEDERATION
IN SUPPORT OF RESPONDENTS**

California Farm Bureau Federation respectfully submits this brief *amicus curiae* in support of Respondents' position in this case.

**INTEREST OF AMICUS CURIAE AND
SUMMARY OF ARGUMENT**

A statement describing California Farm Bureau Federation and its interest in this case is set forth in the preceding motion requesting leave to file this brief *amicus curiae*. Likewise, a summary of the following argument is set forth in the preceding motion under the heading "Summary of the Brief *Amicus Curiae*."

ARGUMENT

I

**PROVIDING GROUP INSURANCE PROGRAMS TO
THEIR MEMBERS IS A KEY PURPOSE OF CALIFOR-
NIA FARM BUREAU FEDERATION AND OTHER NON-
PROFIT ORGANIZATIONS**

The purposes of California Farm Bureau Federation, as set forth in its Articles of Incorporation and Bylaws, include the following:

- (a) To work for the solution of the problems of the farm, the farm home, and the rural community, by use of the recognized advantages of organized action, to the end that those engaged in the various branches of agriculture may have opportunity for happiness and prosperity in their work.
- (b) To represent, protect, and advance the social, economic and educational interests of the farmers of California.

Articles of Incorporation, Art. II; Bylaws, Art. I.

In addition, the Bylaws of California Farm Bureau Federation provide for the creation of a Rural Health Department as an integral part of the corporation. The California Farm Bureau Rural Health Department has been organized:

- (a) To establish working relationships between county medical societies, rural and public health committees and County Farm Bureau Rural Health Departments.
- (b) To work with the health care and social problems of the retired and disabled of the community.
- (c) To work with groups or agencies providing emergency medical services and distribution of health manpower.
- (d) To help County Farm Bureau Rural Health Departments develop a program of work to meet local health and safety needs.
- (e) To work with the health systems agencies at the county, regional and state levels.
- (f) To sponsor health insurance plans and programs.

Bylaws Art. XI, § 1.

California Farm Bureau Federation is the master policyholder for individual members of its member county Farm Bureaus who choose to participate in a workers' compensation insurance program offered by the State Compensation Insurance Fund. As master policyholder, California Farm Bureau Federation guarantees the payment to the State Compensation Insurance Fund of the insurance premiums payable by its participating members. The State Compensation Insurance Fund sells the policies, bills and collects the premiums, processes claims, and provides calculations for distribution of the annual dividend, if any. These dividends constitute a rebate of premiums based on the experience rating and safety record of the master policyholder and members of its member county Farm Bureaus participating in the program.

As master policyholder, California Farm Bureau Federation receives the annual dividend from the State Compensation Insurance Fund. Amounts received as dividends are then distributed to the various county Farm Bureaus (approximately 1.0% of net dividends) to cover their administrative costs, and to their individual members who participate in the program. California Farm Bureau Federation retains a small percentage of the dividend to cover its expenses in administering the program as master policyholder.

The workers' compensation insurance program in which California Farm Bureau Federation has participated for many years is one which is governed by California statutes and administrative regulations. CAL. INS. CODE § 11656.5 (Deering) ordains such a program for the public purpose of permitting employees of small farms to be brought under the provisions of the workers' compensation insurance law. The Insurance Code provides that employers of agricultural labor who are members of any nonprofit agricultural association may, under such conditions as may be prescribed, be insured under a group workers' compensation insurance policy, provided that the agricultural association guarantees the payment of premiums in respect to all members who are covered under the policy. CAL. INS. CODE § 11656.6 (Deering) provides additional requirements with respect to the issuance

of a workers' compensation insurance policy to an association of employers.

The statutory framework set forth above discloses the fact that California Farm Bureau Federation could not participate in this statutory scheme unless it were to (a) act as master policyholder and (b) guarantee the payment of all premiums payable by the insured agricultural employers. Also, the insured agricultural employers could not participate in the statutory scheme unless they were insured under the master policy of California Farm Bureau Federation or the master policy of some other nonprofit agricultural association. Clearly, in order for California Farm Bureau Federation to be true to its purposes of advancing the interests of California farmers through the use of organized action, it was incumbent upon it to sponsor this group insurance program. This, then, is the principal and dominant motive behind the participation of California Farm Bureau Federation in the workers' compensation insurance program. The recognition of any income as a result of its participation in the program is merely incidental, as shown below.

As mentioned earlier, the group workers' compensation insurance program offered by the State Compensation Insurance Fund is highly regulated by California statutes and regulations. One such rule is contained in tit. 10, CAL. ADMIN. CODE § 2508. It requires the articles of incorporation, bylaws, agreements of association, or other rules and regulations filed by a master policyholder to provide that any distribution of funds to any member derived from a dividend shall not be reduced or forfeited except for reasons set forth in the articles of incorporation, bylaws, agreements of association, or rules and regulations of the organization, and no such reduction or forfeiture shall be made unless the reasons for such reduction or forfeiture have been made known to the members by written communication. The effect of this rule, with which California Farm Bureau Federation has complied in all respects, is to make the nonprofit master policyholder a mere trustee of any dividends it retains. As such trustee, California Farm Bureau Federation is required to make known its practices in retaining any dividends distributed to it under the workers' compensation insurance program. Thus, any

dividends retained by it are kept with the full knowledge of the participating members of its member county Farm Bureaus, thereby making these amounts less in the nature of income and more in the nature of contributions from those members to it.

The rules governing the workers' compensation insurance program make it clear that the generation of profit is not the dominant motive behind California Farm Bureau Federation's participation in the program. Any amounts retained by it are kept with the full knowledge of its members who may act together to have such amounts reduced or eliminated. Viewing the program as a whole, it is clear that California Farm Bureau Federation could be compelled to participate in the program as a master policyholder for the benefit of the members of its member county Farm Bureaus regardless of whether any profit were to be gained from its activity. In this context, its activity cannot be termed a "trade or business."

The activity contributes importantly to California Farm Bureau Federation's exempt functions insofar as the program directly promotes rural and agricultural safety programs designed to minimize the danger of injury in farming operations. Thus, this is a group activity which enhances the happiness and prosperity of California farmers and falls within the scope of California Farm Bureau Federation's exempt purposes.

In addition to the workers' compensation insurance program, California Farm Bureau Federation sponsors certain group health and life insurance programs underwritten by CalFarm Life Insurance Company, a separate taxable corporation. Participation in these programs is limited to members of California Farm Bureau Federation's member county Farm Bureaus, their families and workers. California Farm Bureau Federation collects from those members the premiums due under the plans. These amounts are then remitted to CalFarm Life Insurance Company, less 2.2 percent of the estimated gross monthly premiums. California Farm Bureau Federation retains this 2.2 percent of estimated gross premiums under an agreement with CalFarm Life Insurance Company which specifically limits the amounts to be received by California Farm Bureau Federation to those sufficient to cover its costs in collecting the premiums and performing

certain related administrative functions with respect to the programs. California Farm Bureau Federation has undertaken its health and life insurance activities without any intention to produce, or even to generate a right to receive, any "income" or "profit." The 2.2 percent of gross premiums measure is obviously intended to be a rough approximation of costs that may, over any particular period, be greater or less than actual costs, as measured by a refined accounting system. If this rough approximation proves to be incorrect over time, the parties have agreed to adjust the rate to cover only California Farm Bureau Federation's costs.

The Bylaws of California Farm Bureau Federation, *supra*, provide that the betterment of the conditions of those engaged in agricultural pursuits is one of its purposes, as is the protection and advancement of the economic interests of farmers of California, and that these interests are to be pursued through the use of the recognized advantages of organized action. In addition, California Farm Bureau Federation's Bylaws specifically acknowledge that a California Farm Bureau Rural Health Department shall be an integral part of the corporation and shall be organized for the purpose of sponsoring rural health programs, including health insurance plans and programs. Bylaws, Art. XI, § 1.

From the plain meaning of the words of the Bylaws of California Farm Bureau Federation, it is evident that the purposes for which it has been granted exemption from tax include its sponsorship of organized activities that will further the economic interests of California farmers. There can be no doubt that California Farm Bureau Federation's sponsorship and coordination of the life and health insurance programs made available to its members fall within this category. The offering of group insurance benefits to its members, many of whom are self-employed and therefore not eligible to participate in some group insurance plans, is clearly consistent with and substantially related to the stated purposes of California Farm Bureau Federation.

California Farm Bureau Federation believes that adoption by the Court of the position urged by the United States in the case at bar could result in an enormous burden on it if the Court's decision were to cause incidental income received by it from its sponsorship of these group insurance programs to be taxable as

unrelated business income. Likewise, California Farm Bureau Federation believes that the group insurance programs sponsored by many other nonprofit organizations throughout the country in furtherance of their tax-exempt purposes could be jeopardized or, at the least, unfairly taxed, if the Court were to reverse the decision of the court below.

ii

THE COURT SHOULD NOT ADDRESS THE PERIPHERAL ISSUE REGARDING THE RELATION OF THE ACTIVITY TO THE ORGANIZATION'S TAX-EXEMPT PURPOSES

The arguments raised by the United States in this case, if accepted without qualification, would permit a holding which fails to recognize the particular circumstances of California Farm Bureau Federation and similar agricultural associations which sponsor workers' compensation insurance programs.

In the present case the American Bar Endowment evidently has conceded that its group insurance activities are not substantially related to its tax-exempt purposes. *American Bar Endowment v. United States*, 761 F.2d 1573, 1576 (Fed. Cir. 1985). This is not true of the workers' compensation insurance program of California Farm Bureau Federation.

As explained *supra*, CAL. INS. CODE § 11656.5 *et seq.* (Deering) provides that members of any non-public agricultural association may be insured under a group workers' compensation policy, provided that certain requirements are met. The purpose and effect of this provision is to make such insurance available to small farmers with few employees, and the implementation of this goal has been a principal purpose of California Farm Bureau Federation for many years.

Administrative regulations and practice have integrated California Farm Bureau Federation with the accomplishment of this public policy. For example, from the inception of the State Compensation Insurance Fund, its Board of Directors has usually

included a current officer of the California Farm Bureau Federation. Often, this has been its President.

These are, in brief, the particular circumstances which, as stated above, might be ignored if a principal argument made by the United States in the present case were accepted without qualification, and we respectfully urge the Court not to do so.

The argument in question begins with the proposition that insurance activities constitute a trade or business and includes the suggestion that unless such activities are listed in I.R.C. § 501(c) as one of the tax-exempt purposes permitted to a specific kind of organization, the activities are taxable. Brief for the United States at 21.

Thus, the United States notes that fraternal beneficiary societies (I.R.C. § 501(c)(8)) and voluntary employees' societies (I.R.C. § 501(c)(9)) are authorized to provide for life, sickness, accident and other benefits to members. The United States acknowledges that income from such activities is not taxable to these organizations because it is substantially related to their tax-exempt purposes.

The same conclusion should follow even if the tax-exempt purpose is not specifically set forth in I.R.C. § 501(c) but instead is part of a state statutory program, such as the California Farm Bureau Federation's participation in California's workers' compensation insurance program.

The United States, however, suggests an opposite conclusion in its Brief, pointing out that because veterans' organizations were not similarly identified in I.R.C. § 501(c) prior to a statutory amendment in 1972, they "lacked any obvious basis for contending that their insurance operations were 'substantially related' to their exempt functions." Brief of the United States at 21.

The statement quoted above would not by its literal terms preclude California Farm Bureau Federation from establishing that it had an "obvious basis" for contending that its insurance operations were substantially related to its exempt function. However, the United States goes on to argue (*Id.* at 24) that the retroactive amendment of I.R.C. § 512(a)(4) in 1972 shows a

Congressional intent to preclude an organization such as California Farm Bureau Federation from establishing its contention.

This argument goes beyond the issues raised in this case and is irrelevant to it because the American Bar Endowment evidently has conceded that its insurance activities are not substantially related to its tax-exempt purposes. However, the issue is essential to California Farm Bureau Federation in its presently pending controversy with the Internal Revenue Service regarding unrelated business income.

We respectfully submit that the Court should not address this peripheral issue in the present case but should defer it for adjudication, if necessary, upon a fully developed record and briefing by an organization to which it is of the greatest importance.

CONCLUSION

In the case at bar, the United States Court of Appeals for the Federal Circuit correctly held that dividends on a group life insurance policy which insurance carriers had refunded to respondent American Bar Endowment and which it kept pursuant to assignment by its participating members do not constitute taxable unrelated business income. A contrary holding by this Court would greatly harm a multitude of worthwhile group insurance programs operated by nonprofit organizations throughout the country, including those of *amicus curiae* California Farm Bureau Federation.

WHEREFORE, California Farm Bureau Federation respectfully prays that the Court affirm the judgment below.

Respectfully submitted,

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